



DEPARTMENT OF THE ARMY
US ARMY MEDICAL RESEARCH ACQUISITION ACTIVITY
820 CHANDLER STREET
FORT DETRICK, MD 21702-5014

MCMR-AAZ

07 February 2007

MEMORANDUM FOR SEE DISTRIBUTION

SUBJECT: Procurement Advisory Notice (PAN) 07-01
Preparation and Use of the Independent Government Cost Estimate (IGCE)

1. **Introduction.** The IGCE is the Government's estimate of the resources and the projected cost of those resources a prudent contractor will incur in the performance of a contract. These costs include **direct costs** (e.g., labor, supplies, equipment, and transportation) and **indirect costs** (e.g., labor burden, overhead, general and administrative (G&A) expenses, and profit or fee). Development of the IGCE is the responsibility of the requiring activity with assistance, when requested, from the US Army Medical Research Acquisition Activity (USAMRAA), and is used to establish a realistic price/cost for budget purposes. The IGCE is a procurement sensitive document and should be handled accordingly. Access to the IGCE shall be on a need to know basis.

2. **Background.**

a. Subsection 15.404-1 of the Federal Acquisition Regulation charges the contracting officer with the responsibility for evaluating the soundness of offered prices to ensure the final agreed to price is fair and reasonable. The IGCE is one of many tools a contracting officer uses for this purpose. In some cases, the Government's assessment of an offeror's quality and price may be based solely on the IGCE. Any significant variations between cost elements of an offered price and the IGCE requires analysis since parts of the IGCE for many acquisitions, including first time procurements, are based to a degree on uncertainties. However, just knowing where uncertainties exist allows the IGCE to be a useful tool in the evaluation process and in the determination of a fair and reasonable price.

b. The information contained herein is not intended to cover every possible acquisition, but rather explains elements of cost within the general context of their use. Complicated, large dollar acquisitions could contain dozens of cost elements while there could be but a few in the acquisition of a single item, lesser dollar procurement. While the following explanations and descriptions of cost elements are sound, the IGCE should include only those applicable to and developed from the statement of work for the services or construction to be performed or the description of the product to be acquired.

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3. **Applicability.** Although the IGCE is a valuable part of the Government's procurement cycle when utilized, there is no statutory or regulatory site demanding its creation or explaining its preparation. There is no specific monetary threshold or particular contract type that precipitates the formulation of this document. Rather, it is employed whenever required by the contracting officer to create and support an offer evaluation position or when the requiring activity believes the document benefits in reaching the ultimate fairness and reasonableness of price determination.

4. **Overview.** Within the US Army Medical Research and Materiel Command (USAMRMC), the preponderance of IGCEs presented are for services requirements. Thus, the focus of this PAN is the creation of IGCEs for such requirements. An IGCE for a service contract will normally contain the following elements of cost in the chronological order denoted:

- (1) - Direct Labor Costs
- (2) - Labor Burden
- (3) - Other Direct Costs
- (4) - Overhead
- (5) - G&A
- (6) - Profit/Fee

5. **Formation of IGCE.**

a. **Direct Labor Costs** - Labor costs are always the most significant part of the IGCE in terms of dollars for services requirements. Labor costs are incurred in two ways; direct and indirect. Direct labor is the labor directly applied to the specific performance of contract requirements while indirect labor includes costs of personnel in a support capacity that augment the direct performance of the service contracted. For example, for a software development contract being performed at a Command location, the on-site software engineer spending 100% of his work time developing the needed software is direct labor. The project manager overseeing the efforts of the software engineer who spends 50% of his total working time on this contract is also considered direct labor. However, the secretary located in the firm's home office whom very infrequently prepares and transmits correspondence regarding this contract and whose corporate time is spent almost entirely on endeavors not associated with this contract is indirect labor. This segment of the IGCE is devoted to direct labor only. Indirect labor costs are captured in the portion called overhead.

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The IGCE must consider the realities of the work environment. Benefits, including leave and holidays, are part of the contract and must be included into the cost of any Government contract. To develop costs for a typical service contract year, use 1,880 hours (2080 hours less 80 hours holiday, 80 hours vacation, and 40 hours sick leave). This figure can be adjusted downward for part-time labor or for those instances when full coverage must be furnished every day of the year, the figure can be increased to as much as 2080 hours.

Wage rates for each category of direct labor employee must be estimated. Wage rates can be obtained in a number of ways. One source is the Department of Labor's on-line wage rate information that furnishes a listing of occupations and the minimum they are paid by geographical area. If the requirement is already under contract, labor categories and wage rates will be in the existing contract and can be used as a premise for projecting new categories and rates. Salary.com is an available research service for locating wage information. Finally, another source of wage data is the Government's own rates of pay for same or similar labor categories as those forecasted as being needed.

b. Labor Burden (Fringe Benefits).

Sometimes also called payroll additives, labor burden is the percentage of costs for direct labor associated with employee benefits. The benefits that most commonly comprise this cost element are: Health and Welfare, Federal Insurance Contributions Act, Federal Unemployment Taxes; State Unemployment Taxes; and Workers' Compensation. Rather than encumbering the IGCE preparer with the separate computations of these benefits, it is recommended that a straight-line approach using an average overall burden rate of 30 - 35% of the total for direct labor costs be used to compute the labor burden.

c. Other Direct Costs.

This portion of the IGCE provides an estimate of the types and quantities of materials, equipment, travel, etc. necessary for the contractor to perform the work under the awarded instrument. These are costs that can be charged directly against the specific requirement.

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Normal office supplies are generally included in overhead or G&A, but any materials used in direct support of the contract, such as vehicles, computers, office furniture, subcontractor costs, lease of equipment, etc. should be included

in this cost element. Item descriptions, quantities, and related cost estimates can be obtained using catalogs, price quotes, market surveys, historical data, etc.

Estimates for required travel includes the number of trips (to and from), the number of personnel required to make the trips, the purpose of the trips, the expected number of days required, as well as air fares, rental car needs, and per diem costs. The dollars associated with travel can be roughly estimated.

d. Overhead.

This category includes all overhead and other indirect costs that cannot be specifically applied to a cost category but is in support of the contracted service. Overhead includes expenses such as utilities, rent, janitorial supplies, office supplies, transportation, and depreciation.

Overhead is expressed as a percentage of the sum of labor costs, labor burden, and other direct costs. Although overhead will vary based on type of contract, ownership of facilities, location of work site, etc., it is recommended that a straight-line approach using an average of 15% be used for this calculation.

e. G&A.

G&A costs are those borne by all elements of a company not associated with one particular project. They are any management, financial or other expenses incurred for the overall operation of a business. Examples of some of elements of G&A are compensation packages, employee training, jury duty, business taxes, legal costs, and liability and other business insurances. These costs are distributed equally across all contracts, Government and private sector.

G&A is expressed as a percentage of the sum of all other expenses (labor, labor burden, other direct costs, and overhead). Typical G&A rates range between 12 - 15 %. It is recommended the IGCE preparer utilize a straight-line approach using a figure of 15% for this computation.

f. Profit/Fee.

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Profit represents the monetary excess realized by a contractor after the deduction of costs incurred. Fee represents a pre-determined amount beyond the initial estimate of cost. Predominantly, contracts awarded for USAMRMC set the profit/fee at the outset of the contract as when a firm-fixed-price contract or a cost-plus-fixed-fee contract is established. However, on occasion, the profit or

fee may vary during the course of a contract as in a fixed-price incentive contract or a cost-plus-award fee instrument.

The size of the acquisition, in terms of both risk and difficulty, are primary considerations in the determination of a profit/fee. It is recommended the IGCE preparer research previously submitted IGCEs and subsequent negotiation memorandums/award decision documents for same or similar services to assist in the arrival of a profit/fee objective for the forthcoming requirement. In the absence of any such data, a straight-line approach to profit/fee establishment is recommended. A profit of 10% for a firm-fixed-price service contract is a credible recommendation while a fee of 6% for a cost-plus-fixed-fee service contract is plausible.

g. Escalation.

The impact of escalation must be considered when developing the IGCE. Two methodologies that can be used to project escalation are market research and the Department of Labor Consumer Price Index (CPI).

A market survey will provide information on current market prices and the potential volatility of prices in the market place. Also, a review of Treasury interest rates will help provide an overall view of market prices.

The CPI, found at <http://www.bls.gov/cpi/>, provides data and percentage of change in inflation factors. When projecting inflation, a review of the major cost factors for the specific requirement as well as the geographic locations for work performance will aid in the creation of escalation estimates.

Data collected from the past decade has shown a percentage of change for the collective items of cost ranging from a low of about 1.5% to a high of approximately 3.5%. Thus, an escalation rate of approximately 2% - 4% per year advocated by the IGCE preparer should normally be considered acceptable.

6. Straight-Line Rate Reviews. The straight-line indirect cost percentages included in this PAN are estimates derived from acquisition history. USAMRAA

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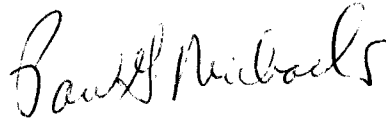
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will sample actual cost rates each fiscal year and will update this PAN with newer, more accurate estimates if the sample indicates actual rates differ significantly from the percentages included herein.

7. **Sample IGCE.** A sample IGCE, prepared in consonance with the offerings of this PAN, appears as Attachment A.

8. **Point of Contact.** Raegon B. Clutz, Chief, Policy Branch, US Army medical Research Acquisition Activity, 301-619-2395, AV 343-2395, or e-mail raegon.clutz@det.amedd.army.mil.



PAUL G. MICHAELS

Principal Assistant

Responsible for Contracting

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DIST A & D

Attachment A

Independent Government Cost Estimate for Software Engineering Services

For Official Use Only

Procurement Sensitive - Source Selection Information

Base Year: January 1, 2007 - December 31, 2007

Direct Labor (DL)

<u>Labor Category</u>	<u>Hours</u>	<u>Rate</u>	<u>Amount</u>
Senior Software Engineer	1880	45.00	84,600.00
Senior Software Engineer	1410	45.00	63,450.00
Junior Software Engineer	1880	35.00	65,800.00
Program Manager	470	65.00	30,550.00
Total DL			<hr/> \$244,400.00

Labor Burden (LB; 35%)

	244,400.00
	x .35
	<hr/>
Total LB	\$85,540.00
Total DL and LB	\$329,940.00

Other Direct Costs ODCs)

Three (3) Dell desktop computers with printers @ \$2,900.00/each	8,700.00
Three (3) software licenses MEDSEARCH SOFTWARE @ \$1,200.00/each	3,600.00
Three Memberships - National Society of DoD Software Developers @ 1,000.00/each	3,000.00
Travel - Three projected trips (May, July, and	7,800.00

November 2007), Monday - Friday, for full time Senior Software Engineer from Frederick, MD to Chicago, IL and return. Airfare; lodging, car rental, and per diem estimated at \$2,600/trip.

Total ODCs	\$23,100.00
Total DL, LB, and ODCs	\$353,040.00

Overhead (OH;15%)

\$353,040.00
x .15

Total OH	\$52,956.00
Total DL, LB, ODCs, and OH	\$405,996.00

G&A (12%)

\$405,996.00
x .12

Total G&A	\$48,720.00
Total DL, LB, ODCs, OH, and G&A	\$454,716.00

Profit (10% -FFP)

\$454,716.00
x .10

Total Profit	\$45,472.00
Total DL, LB, ODCs, OH, G&A, and Profit	\$500,188.00

Escalation

3 % per year for option year 1 and option year 2

Base Year (January 1, 2007 - December 31, 2007)	500,188.00
Option Year 1 (January 1, 2008 - December 31, 2008)	515,194.00
Option Year 2 (January 1, 2009 - December 31, 2009)	530,649.00

Total All Years	\$1,546,032.00
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Prepared by:_____ Approved by:_____

Signature_____ Signature_____